FILE COPY

OCT 10 1935

Supreme Court of the United States

OCTOBER TERM, 1935.

No. 10

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

CITY BANK FARMERS TRUST COMPANY, as Trustee under an agreement with Gertrude Feldman James, Deceased.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT.

RUSSELL L. BRADFORD,
Attorney for Respondent,
20 Exchange Place,
New York City.

CARL TAYLOR,
GEORGE H. CRAVEN,
MITCHELL, TAYLOR, CAPRON & MARSH,
20 Exchange Place,
New York City,
Of Counsel.

INDEX.

	PAGE
THE QUESTION PRESENTED	1
THE STATUTE INVOLVED	1
STATEMENT	2
SUMMARY OF ARGUMENT	3
ARGUMENT:	
POINT I. Section 302(d) does not and was not intended to apply to transfers or trusts revocable only with the consent of one having a beneficial and consequently adverse interest	4
(a) A power dependent upon the consent of an interest adverse to its exercise is no power, and Congress did not intend the statute to apply in such a case	12
(b) The rule that a statute will be construed so as to relieve it of unconstitutionality and even to avoid a serious doubt thereof, is applicable here	15
POINT II. The statute if construed to apply to the facts in suit is unconstitutional	20
POINT III. No part of the trust fund is subject to the tax	24
CONCLUSION	26

Table of Cases.

	PAGE
Barstow, Matter of, 230 App. Div. 371, aff'd 256 N. Y. 647	14
Blodgett v. *Holden*, 275 U. S. 142	4, 16
Burnet v. *Guggenheim*, 288 U. S. 280	7, 15
Burnet v. *Northern Trust Co.*, 283 U. S. 782	22
Chase National Bank v. *United States*, 278 U. S. 327	17
Church of the Holy Trinity v. *United States*, 143 U. S. 457	17
Commissioner v. *Stevens* (decided Sept. 17, 1935, C. C. A. 3, unofficially reported in Commerce Clearing House F. T. S. at p. 10,425)	25
Commissioner v. *Strauss*, 77 F. [2d] 401	19
Cram v. *Walker*, 173 App. Div. 804, 806	12
Edwards v. *Slocum*, 264 U. S. 61	20
Farmers' Loan & Trust Co. v. *Minnesota*, 280 U. S. 204	3
Frew v. *Bowers*, 12 F. [2d] 625	23
Garner v. *Germania Life Ins. Co.*, 110 N. Y. 266	12
Heiner v. *Donnan*, 285 U. S. 312	5, 19, 20, 22, 23
Helvering v. *Helmholz*, 75 F. [2d] 245	25
Hoeper v. *Tax Commission*, 284 U. S. 206	19, 23
Knowlton v. *Moore*, 178 U. S. 41	20, 23
Levy v. *Wardell*, 258 U. S. 542	17
Lewellyn v. *Frick*, 268 U. S. 238	4, 16
Lit v. *Commissioner*, 72 F. [2d] 551	24
May v. *Heiner*, 281 U. S. 238	5, 18, 20, 22
McCormick v. *Burnet*, 283 U. S. 784	4, 6, 8, 10, 25

PAGE

Milliken v. *United States*, 283 U. S. 15 ..... 5, 20
Moore v. *Littel*, 41 N. Y. 66 14
Morsman v. *Burnet*, 283 U. S. 783 22

Nichols v. *Coolidge*, 274 U. S. 531 ..... 3, 18

Panama R. R. Co. v. *Johnson*, 264 U. S. 375 ..... 4, 16
Porter v. *Commissioner*, 288 U. S. 436
3, 4, 5, 9, 10, 11, 12, 14, 19, 21

Reinecke v. *Northern Trust Co.*, 278 U. S. 339
3, 4, 5, 8, 9, 10, 11, 12, 14, 21, 23, 25
Reinecke v. *Smith*, 289 U. S. 172 ..... 3, 4, 6, 11, 14

Schlesinger v. *Wisconsin*, 270 U. S. 230 ..... 19, 23
Schmidlapp, Matter of, 236 N. Y. 278 6
Shwab v. *Doyle*, 258 U. S. 529 17

Tyler v. *United States*, 281 U. S. 497 ..... 5, 21

Union Trust Co. v. *Wardell*, 258 U. S. 537 17
United States v. *Delaware & Hudson Co.*, 213 U. S. 366 16
United States v. *Jin Fuey Moy*, 241 U. S. 394 ..... 4, 16, 17
United States v. *Kirby*, 7 Wall. 482 [74 U. S.] 17

White v. *Poor*, 75 F. (2d) 35 ..... 10, 13
Witherbee v. *Commissioner*, 70 F. [2d] 696, certiorari denied 293 U. S. 582 12

Y. M. C. A. v. *Davis*, 264 U. S. 47 20

Other Authorities Cited.

PAGE

Personal Property Law of New York:

Sec. 11 14
Sec. 23 12

Real Property Law of New York, Sec. 40 14

Regulations 79, Art. 3 13

Regulations 80, Art. 27 17

Report Ways and Means Committee, 73rd Cong., 2nd Session, H. R. 704, p. 40 15

Revenue Act of 1926:

Sec. 302 (d) 1, 2, 4, 5, 9, 18, 24
Sec. 302 (g) 17

Revenue Act of 1932, Sec. 501 (c) 15

SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM, 1935.

No. 10.

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

CITY BANK FARMERS TRUST COMPANY, as Trustee under an agreement with Gertrude Feldman James, Deceased.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT.

The Question Presented.

The issue is (1) whether Section 302(d) of the Revenue Act of 1926 may be construed so as to apply to an *inter vivos* trust unalterable and irrevocable, except with the consent of a beneficiary and consequently an interest adverse to such alteration or revocation; and (2) whether, if it may be so construed, it is not unconstitutional as in violation of the due process of law clause of the Fifth Amendment of the Federal Constitution.

The Statute Involved.

Revenue Act of 1926, c. 27, 44 Stat. 9, 70:

> Sec. 302. The value of the gross estate of the decedent shall be determined by including the value

at the time of his death of all property, real or personal, tangible or intangible, wherever situated—

* * * * * * *

(d) To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, * * *.

Statement.

Gertrude Feldman James, a non-resident of the United States, died May 20, 1931 (R. 13). On February 21, 1930, she created a trust with the City Bank Farmers Trust Company of New York, as trustee (R. 13). Every security in the trust was a foreign security (R. 20-22). The trust was to continue during the lives of her two daughters or the survivor (R. 13). The income of the trust was to be paid to her during her life or until the termination of the trust (R. 13). After her death, her husband, Samuel James, surviving, the income was to be paid to him. If he were dead, or upon his death, the income was to be paid to the two children, or the descendants, if any, of such child as might be then dead (R. 4).

Upon the termination of the trust the principal was to be paid to Samuel James (the husband) if he were then alive (whether or not the Settlor was still living) and if he were then dead, to the Settlor if she were alive, if not, then to the descendants of the two children, and if none, then to heirs at law of Samuel James (R. 5).

The trust was unalterable and irrevocable except with the written consent of the trustee and Samuel James during his life, and after his death except with the written consent of the trustee and Samuel James' brother (R. 7). Samuel James, the husband, survived, and is now receiving the income of the trust (R. 15).

The trust indenture also provided (R. 5) that during the trust term the trustee could from time to time in its discretion apply to the use of the husband and his descendants so much of the principal of the trust as it deemed advisable for their proper education, care, comfort, support, or advancement in life.

Summary of Argument.

A transfer or trust subject to no revocation or alteration except with the consent of a "beneficial, and consequently adverse, interest" is complete when made (*Reinecke* v. *Northern Trust Co.*, 278 U. S. 339, 346, and cf. *Reinecke* v. *Smith*, 289 U. S. 172, at p. 176).

A power exercisable only upon or with the consent of one adverse to such exercise is in effect "for all practical purposes" no power at all. If no power in the Settlor existed at her death by which she could in any reasonable, practical sense, revoke or change the beneficial interests already fixed and determined, the statute could not and was not intended to have application.

"Taxation is an intensely practical matter" (*Farmers' Loan & Trust Co.* v. *Minnesota*, 280 U. S. 204, 212), and laws in respect of it should be construed and applied in a practical, reasonable way. "Taxes are very real things and statutes imposing them are estimated by practical results" (*Nichols* v. *Coolidge*, 274 U. S. 531, 541). The statute in suit should be construed reasonably, and practically, in the light of the fundamental law.

In view of the decision of this Court in *Reinecke* v. *Northern Trust Co.*, *supra*, and the re-announcement in *Porter* v. *Commissioner* (288 U. S. 436), and *Reinecke* v. *Smith* (289 U. S. 172) of the doctrine there laid down, serious constitutional questions are presented if the statute may be construed so as to apply to an *inter vivos* transfer, not made in contemplation of death, and irrevocable except with the consent of a beneficial or adverse interest.

"Even to avoid a serious doubt" (*Blodgett* v. *Holden*, 275 U. S. 142, 148) that construction should be given that will save the Act (*Lewellyn* v. *Frick*, 268 U. S. 238, 251; *Panama R.R. Co.* v. *Johnson*, 264 U. S. 375, 390; *United States* v. *Jin Fuey Moy*, 241 U. S. 394, 401, 402).

But if the statute is susceptible of no construction other than that contended for by the Commissioner of Internal Revenue, then the statute, it is submitted, as applied to the facts in suit, is arbitrary and capricious, and in violation of the due process of law clause of the Fifth Amendment of the Federal Constitution.

ARGUMENT.

POINT I.

Section 302(d) does not and was not intended to apply to transfers or trusts revocable only with the consent of one having a beneficial and consequently adverse interest.

The statute (Sec. 302(d) Rev. Act of 1926) provides for the inclusion in the gross estate of a decedent of any property transferred or trust created "where the enjoyment thereof was subject *at the date of his death* to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke * * *". (Italics ours.) It is clear that the statute must be reasonably construed in the light of the fundamental law. This Court has held that a so-called power so conditioned and bridled did not bring the transfer within the taxing statute there involved (*Reinecke* v. *Northern Trust Co.*, supra; *McCormick* v. *Burnet*, 283 U. S. 784, and *cf. Porter* v. *Commissioner*, supra, pp. 443, 444, and *Reinecke* v. *Smith*, supra, 176, 177). It was in accordance with the opinions in these cases that the Circuit Court of Appeals below consonantly decided the case in suit. The fundamental and thoroughgoing nature of the doctrine laid down in the

above referred to cases is too inherent in the scheme of the law itself to be confined only to the section of the law passed upon in *Reinecke* v. *Northern Trust Co.*, supra.

It is fundamental that a completed *inter vivos* transfer, not made in contemplation of death, may not be subject to the Federal estate tax as a part of the gross estate of the decedent (*Heiner* v. *Donnan*, 285 U. S. 312; *May* v. *Heiner*, 281 U. S. 238). A transfer the *control of the disposition of which* is retained by the transferror to the time of death is properly the subject of tax, whether the control of that disposition be one beneficial to the settlor (as in *Reinecke* v. *Northern Trust Co.*, supra,—two trusts), or non-beneficial to himself or his estate (as in *Porter* v. *Commissioner*, supra). An estate by the entirety or a joint tenancy is amenable to the taxing law (*Tyler* v. *United States*, 281 U. S. 497). There, a property right obtaining in the decedent at the moment of death does indeed, this Court held, accrue to the survivor—and death thus was the occasion of the shifting of economic benefits from one of the entirety to the survivor—moving by reason of death from the dead to the living, which is the incidence of the tax. Gifts made in contemplation of death (*Milliken* v. *United States*, 283 U. S. 15), while not made at death, are nevertheless so assimilated to death by reason of the fact that the transfer would not have been made for the coercive motive of contemplated death, that it seemed the property passed from the dead to the living within the purview of the statute.

But here nothing passed from Mrs. James at her death or by reason of her death to anyone else. Her life interest in the income of the trust was merely obliterated by her death (*May* v. *Heiner*, 281 U. S. 238, 243). The transfer concededly was not made in contemplation of death. The only ground upon which it is sought to be taxed is under the provisions of Section 302(d). Indeed, if she had not created the trust there would have been no claim for the tax, because the foreign securities, if with her at her

domicile abroad, were not taxable in the United States. The property rights were fixed and determined by the deed of transfer on February 21, 1930, and were fixed on that date long prior to death. "The tax is a charge upon the creation of the right. It is not a charge upon fruition in enjoyment or possession. We must fix the point of time at which creation was effective". (Cardozo, J., in respect of the New York transfer tax in *Matter of Schmidlapp*, 236 N. Y. 278, at p. 283, and see relatively the same thought expressed by Mr. Justice Roberts in *Reinecke* v. *Smith*, 289 U. S. at p. 176.) Upon Mrs. James' death her husband, pursuant to the terms of the trust instrument, became the life tenant and is now receiving the full income of the trust (R. 15). "We are to view the sequence of events in the order of the actual rather than the possible" (*Matter of Schmidlapp*, at p. 286).

Two cases in this Court, we think, stand as barriers not only to the construction sought by the petitioner, but to the constitutionality of the law if he were successful in having this Court adopt the construction urged by him (*Reinecke* v. *Northern Trust Co.*, *supra*, and *McCormick* v. *Burnet*, 283 U. S. 784).

In *Reinecke* v. *Northern Trust Co.*, which arose under the 1921 Act, and had for consideration Section 402(c) thereof, which taxed transfers intended to take effect in possession or enjoyment at or after death, there were seven trusts created by the decedent during his lifetime. Two were created, respectively, in 1903 and 1910 prior to the enactment of the first Federal Estate Tax law. The other five were all created in 1919 after the enactment of the first Federal Estate Tax law. In each of the first two trusts "there was reserved to the settlor *alone* a power of revocation". (Italics ours.) In each of the remaining five trusts the settlor reserved a power "to alter, change or modify the trust", which power was to be exercised in the case of four of them by the settlor and the single beneficiary of each trust, acting jointly, and in the case of one

of the trusts by the settlor and a majority of the beneficiaries named, acting jointly.

Four of these five trusts were for the benefit, respectively, of the four children of the settlor, and each could be altered or modified only with the consent of the beneficiary of such trust. The fifth was for the life benefit of the wife with remainders over to the four children.* That trust could be altered or modified with the consent of a majority of such five beneficiaries. In other words, three of them, the other two unwilling notwithstanding, could join with the settlor in altering, changing or modifying the trusts created, to the exclusion of the rights or interests of the other two.

This Court held the two trusts of 1903 and 1910 subject to the tax. This, upon the ground that the settlor, until his death, had complete *dominion* and *control over the disposition* of the property to the date of his death, and therefore the transfer was not complete until death. (See and cf. *Burnet* v. *Guggenheim*, 288 U. S. 280.) In the five trusts, however, this Court held the transfers were complete when made (pp. 346-7), and thus not within the taxing ambit. This, we submit, because the basis of the tax, that is, the incidence, is upon the transfer of property, the shifting of economic interests and benefits, from the dead to the living by reason of death, and as the trusts were complete when made nothing remained that passed from the dead to the living at death.

The doctrine there laid down by this Court sinks deep into the roots of the law governing the whole tax scheme. At p. 346, through Mr. Justice Stone, this Court said:

> "He could not effect any change in the beneficial interest in the trusts without the consent, in the case of four of the trusts, of the person entitled to that interest, *and in the case of one trust without the consent of a majority of those* so entitled. *Since the power to revoke or alter* was dependent on the con-

* See Transcript of Record.

> sent of the one entitled to the beneficial, and consequently adverse, interest, *the trust, for all practical purposes, had passed as completely from any control by decedent* which might inure to his own benefit *as if the gift had been absolute.*" (Italics ours.)

And again, at pp. 346-347, the opinion continues:

> "The shifting of the economic interest in the trust property which was the subject of the tax *was thus complete as soon as the trust was made.* His power to recall the property and of control over it for his own benefit then ceased and as the trusts were not made in contemplation of death, the reserved powers do not serve to distinguish them *from any other gift inter vivos not subject to the tax.*" (Italics ours.)

In *McCormick* v. *Burnet* (283 U. S. 784, reversing 43 F. [2d] 277), the settlor created in 1918 a trust, the income to be accumulated and added to principal, except under certain circumstances not here material, during the life of the settlor. Upon her death the income was to be distributed equally among her three children. The settlor reserved the power to terminate the trust in whole or in part at any time by the delivery to the trustee of an instrument signed by her "and by one or more of her three children hereinbefore named". Upon termination of the trust during the settlor's life the principal was to be turned over to her.

This Court held the transfer in trust by Mrs. McCormick not subject to the Federal estate tax under the provisions of Section 402(c) of the Revenue Act of 1921.

The holding and the language in *Reinecke* v. *Northern Trust Company* are too direct, and the principle there laid down too fundamental, to be brushed aside as applying only to the case there decided or the section of the statute there considered, and this seems clear from subsequent decisions of this Court in which that doctrine has been again and again re-announced. That the principle announced in *Reinecke* v. *Northern Trust Company*, and re-applied in *Mc-*

Cormick v. *Burnet* still obtains, and is inherent in the tax scheme itself, is indicated by a decision arising under subdivision (d) of Section 302 (the very section here involved), which case takes not one whit from the fundamental force and nature of the doctrine. *Porter* v. *Commissioner* (288 U. S. 436). In that case the Court held an *inter vivos* transfer taxable where the donor had a power of disposition or appointment to new uses at the time of his death, though not for the benefit of either himself or his estate. This Court held that such a transfer, with such a power of disposition or appointment to new uses reserved *exclusively* to the settlor, brought the transaction within the purview of Section 302(d). This Court at that time was careful to point out that the power in the *Porter* case was indeed a power, that is to say a power that "the donor reserved unto himself alone" (p. 444), while indicating that the so-called power in the *Reinecke* case was impotent and ineffective and for that reason the *Reinecke* case was distinguishable from the *Porter* case.

Mr. Justice Butler in pointing out the inapplicability of the *Reinecke* case to the facts and the statute in the *Porter* case, and in repeating the doctrine expressed in the *Reinecke* case, without in any way emasculating its primary force or shading its meaning, said at p. 442:—

> "Two were held taxable because subject to a power of revocation *in him alone. In each of the others* he reserved power to alter, change or modify, to be exercised in four by joint action of himself and a single beneficiary, and in the remaining one by himself and a majority of the beneficiaries acting jointly. As the title *was put beyond his control, we held these transfers not taxable*". (Italics ours).

This Court then proceeded to point out the basic factor that rendered the transfers in the *Porter* case amenable to the statute, while leaving it clear, we submit, that such a transfer as that in *Reinecke* v. *Northern Trust Company* would not have been, and said at p. 444:—

> "They [the petitioners] treat as without significance *the power the donor reserved unto himself alone* and ground all their arguments upon the fact that deceased, prior to such enactment, completely divested himself of title without power of revocation * * *. But the reservation here may not be ignored, for, while subject to the specified limitation, *it made the settlor dominant in respect of other dispositions of both corpus and income.*" (Italics ours).

The settlor in the case in suit had no such control or dominion. She had even less control and dominion than the settlor in either the *Reinecke* v. *Northern Trust Co.* or *McCormick* v. *Burnet* cases. It will be noted that the decision in the *Porter* case is not only consonant with the decision in *Reinecke* v. *Northern Trust Company,* but the same fundamental doctrine like "a common thread of purpose" runs through both. That doctrine is that so long as a transferror, up to the moment of death, has "control of the disposition" of the property, that is to say, the transferror has the "dominant" right in respect of the disposition, whether self-beneficial or not, it is death that occasions the shifting of economic interests, and is consequently the incidence of the tax. If the settlor be not dominant in the power of disposition at death, and have no power except with consent of an interest necessarily adverse to modification, alteration or revocation, then it may not be said, within the sphere of practicality, that the transferror had any power whatever (see and cf. *White* v. *Poor,* 75 F. (2d) 35, 38, C. C. A. 1, No. 36, here). A power exercisable only with the consent of an adverse interest is not a power, clearly not a power of such strength as to support an excise of the character here presented.

This Court, again, in considering another statute (income tax law) after the decision of *Reinecke* v. *Northern Trust Co.,* pointed out the distinction between a power unrestrained wholly or restrained only by one not having an adverse beneficial interest, and a so-called power exercisable

only upon the consent of an adverse beneficial interest. In *Reinecke* v. *Smith* (289 U. S. 172), this Court, through Mr. Justice ROBERTS, said at p. 176, in reference to *Reinecke* v. *Northern Trust Co.*:—

> "The tax was upheld as applied to the corpus of trusts over which the grantor *had sole power* of revocation. *It was, however, condemned as to those where revocation was dependent upon joint action of the grantor and the beneficiary,* for the reason that the interest of the beneficiary was adverse and the grantor *unable at will* to alter or destroy the trust. *In the latter case the transfer was said to be effective when made, not at death.* As pointed out in *Burnet* v. *Guggenheim* (288 U. S. 280) the same considerations as to ownership and control affect the power to impose a tax on the transfer of the corpus and upon the income." (Italics ours).

Thus again this Court was insistent to reiterate the principle laid down in *Reinecke* v. *Northern Trust Co.* It further said at p. 177:—

> "A settlor who at every moment retains the power to repossess the corpus and enjoy the income has such a measure of control as justifies the imposition of the tax upon him. *Corliss* v. *Bowers,* supra. We think Congress may *with reason* declare that where one has placed his property in trust subject to the right of revocation in himself and another, *not a beneficiary,* he shall be deemed to be in control of the property." (Italics ours).

It thus will be seen that the Court subsequent to the decision of *Porter* v. *Commissioner,* was careful again to lay down the doctrine of the right of the Congress to tax by reason of the reserved control or dominion over the disposition of the property either alone or in conjunction with someone else, but obviously with equal care and deliberation indicated condemnation of the tax if that supposed control was fettered by the necessity of a beneficiary's consent.

(a) *A power dependent upon the consent of an interest adverse to its exercise is no power, and Congress did not intend the statute to apply in such a case.*

Every *inter vivos* trust is subject to revocation with the consent of all the interested parties. It is clearly so under the New York law (*Garner* v. *Germania Life Ins. Co.*, 110 N. Y. 266), and this trust by its terms was governed by the laws of New York (R. 7). It is even provided by statute in New York (Personal Property Law, Sec. 23) that a trust of personal property may be revoked by all persons in interest living at the time uniting in the act, and this has been held to permit the life beneficiary to terminate such a trust even when there may be possible unborn interested parties (see *Cram* v. *Walker*, 173 App. Div. 804, 806).

Any gift is subject to revocation if the donee thereof consents thereto. Unless a fetish be made of literalism, the word "person" could have its roots only in the understanding that the statute had reference to a transfer incomplete so far as the *control and dominion over the disposition* thereof by the settlor was concerned at the time of his death. (see and cf. *Porter* v. *Commissioner*, 288 U. S. 436, 444). So far as the control of the property and its disposition by the settlor was concerned, the trust in suit stood in no different position from that of a trust in which the provisions of Clause 12 thereof were omitted.

The words "any person" could not in reason, under this kind of tax, apply to a donee or adverse beneficiary; and yet a donee is a person. The meaning must apply to strangers to the property rights or beneficial interests. So construed the word is applied to a trustee (*Witherbee* v. *Commissioner*, 70 F. [2d] 696, certiorari denied 293 U. S. 582). There the circuit court of appeals said at p. 697:—

> "The situation is unlike that in *Reinecke* v. *Trust Co.*, 278 U. S. 339, where the power was subject to the approval of the beneficiaries themselves."

And thus the basic thought remains yet plain. A trustee, it has been held, is not a beneficiary (*Reinecke* v. *Smith*, supra), and does not hold an adverse beneficial interest—whatever his duties otherwise may be. But to apply the words to a donee (or other adverse interest) is to include practically every *inter vivos* trust or gift, and render the statute unreasonable and arbitrary. Trusts irrevocable except with the consent of the beneficial adverse interest are taxable under the gift tax law as completed transfers. (See Art. 3, Reg. 79, Gift Tax.)* If, as this Court has held, they are complete at the time of creation, then they are not incomplete later at death.

The practical result of a revocation with the consent of a donee or other adverse beneficial interest is a gift back by the donee or such beneficial adverse interest, and so the Circuit Court of Appeals for the First Circuit said in *White* v. *Poor* (75 F. [2d] 35), at p. 38:

> "In view of the decision in *Reinecke* v. *Northern Trust Company* we are of the opinion that the decedent before and at the time of her death had no power by which she could effect a change of interest in the trust, and consequently that the corpus of the

---

* Art. 3. Transfers in trust.—Where property is transferred in trust without an adequate and full consideration in money or money's worth and without the reservation of the power to revest in the donor title to such property, the transfer is a gift, but, where the donor reserves such power, the transfer does not constitute a gift within the meaning of the statute. * * * For the purposes of these regulations a donor shall be considered as having the power to revest in himself title to the property transferred in trust where he has such power in conjunction with any person not having a substantial adverse interest in the disposition of the trust property or the income therefrom. A trustee, as such, is not a person having a substantial adverse interest in the disposition of the trust property or the income therefrom. Where the power to revest in the donor title to property transferred in trust reposes in him in conjunction *with any other person having a substantial adverse interest* in the disposition of the property or the income therefrom or where the power is in such other person alone, *the transfer is subject to tax* as though no such power existed. (Italics ours.)

trust was completely transferred to the trustee at the date of the execution of the trust instrument, for whatever power was reserved to her could only be exercised in conjunction with one having a beneficial adverse interest. If A gives property to B, reserving to himself the right to revoke the same only upon B's consent, the transfer is complete, the reservation is nil, and whether A gets the property back or not lies wholly with B. If a transfer back is made with B's consent, it would be a gift back and not a revocation. This is in substance the situation here."

It is beyond question, we submit, that Samuel James had an actual, substantial, interest in the trust fund, the corpus as well as the income therefrom. In addition thereto, he was not only the remainderman upon the termination of the trust during his lifetime, but he had also a right to the corpus for his own care, comfort, support or advancement in life, in the discretion of the trustee, during the term of the trust; and furthermore, upon the failure of the remainders set out in the trust, the property went to *his* heirs at law, not the heirs at law of the settlor. His interests were vested interests (Sec. 40 N. Y. Real Property Law; Sec. 11 Personal Property Law; *Moore* v. *Littel*, 41 N. Y. 66; *Matter of Barstow*, 230 App. Div. 371, aff'd without opinion 256 N. Y. 647).

The settlor had no power of revocation, amendment, or alteration at the time of her death within the purview of the statute. The so-called power expressed in the trust indenture lay impotent and ineffectual in her hands. It was only upon the consent of one holding an adverse interest that she could act. An impotent power is no power. That such a power, so conditioned and so circumscribed, does not affect the completeness of the transfer, is clear from the decision in *Reinecke* v. *Northern Trust Co.*, and the reiteration of the doctrine there laid down in *Porter* v. *Commissioner*, *supra*, and in *Reinecke* v. *Smith*, and is indicated in the treatment of such transfers by the Internal

Revenue Bureau in the administration of the Gift Tax laws; and was in words expressed in the 1932 Act (Sec. 501(c))*.

If there was in any practical, reasonable, sense a power of alteration or disposition in anyone during the life of Mrs. James, that power lay in the hands of her husband, the beneficiary. Not in the Settlor. Her act, will, or power was a nullity. Only by the act of Samuel James, the beneficiary, could the trust be altered, amended or revoked. True, this power was not in him alone. Nevertheless, nothing could be done except it be done in accordance with his wishes and consent; and his interests in both the principal and the income were substantial vested adverse interests.

(b) *The rule that a statute will be construed so as to relieve it of unconstitutionality and even to avoid a serious doubt thereof, is applicable here.*

The petitioner argues that there is no room for construction, that the language of the statute is too plain to leave open to this Court the right to construe. We submit that not only is there room for construction, but that any statute, which if literally and slavishly construed would raise grave doubts of its constitutionality, is the subject of reasonable, practical construction by this Court. We further submit that the construction urged herein by us does not superimpose on the language of the statute a qualification not therein contained. Nor does it, under the pretense of construction, in effect seek to amend the statute.

---

* Because of the decision in *Burnet* v. *Guggenheim*, 288 U. S. 280, this section was omitted in the 1934 Act. See Report Ways and Means Committee, 73rd Congress, 2nd Session, H. R. 704, at p. 40, where it is stated:—

> "Sec. 511. Gifts of property subject to power: This section repeals Section 501(c) of the Revenue Act of 1932, since the principle expressed in that section *is now a fundamental part of the law* by virtue of the Supreme Court's decision in the *Guggenheim* case." [Italics ours].

On the contrary, the language, we urge, should be given that construction that is in keeping not only with the tax scheme but with the fundamental law lying at the base of this kind of tax. This is a death tax, not a gift tax.

We submit that the statute should be construed so as to relieve it of any question of constitutionality, or even any doubt upon that score (*Blodgett* v. *Holden*, 275 U. S. 142—concurring opinion of Mr. Justice Holmes, p. 148; *Panama R. R. Co.* v. *Johnson*, 264 U. S. 375, 390; *United States* v. *Jin Fuey Moy*, 241 U. S. 394, 401, 402; *United States* v. *Delaware & Hudson Co.*, 213 U. S. 366, 407, 408).

In *Blodgett* v. *Holden*, supra, it was said at p. 148:

> "* * * The rule is settled that as between two possible interpretations of a statute, by one of which it would be unconstitutional and by the other valid, our plain duty is to adopt that which will save the act. *Even to avoid a serious doubt the rule is the same.*" (Italics ours.) (Concurring opinion Mr. Justice Holmes.)

In *Lewellyn* v. *Frick* (268 U. S. 238), the Court said at p. 251:

> "Acts of Congress are to be construed if possible in such a way as to avoid grave doubts of this kind."

In *Blodgett* v. *Holden* the Revenue Act of 1924 (Sec. 319) had provided for a tax upon all gifts made during the calendar year 1924, although the law was not passed until June 2, 1924. This Court held the tax inapplicable to gifts made before the law was introduced in Congress. Four members placed the decision upon the ground that the fairly plain words of the statute should be construed to mean gifts made during the calendar year 1924 "after the enactment of the law" (p. 148).

The Revenue Act of September 8, 1916 (Sec. 202(b)) had provided that "to the extent of any interest therein of which the decedent *has at any time made a transfer* * * *

in contemplation of death", etc., the transfer was taxable. Yet this Court held that the words "has at any time made a transfer" must be construed to mean "has at any time after the enactment of the act". (*Shwab* v. *Doyle*, 258 U. S. 529; *Union Trust Co.* v. *Wardell*, 258 U. S. 537; *Levy* v. *Wardell*, 258 U. S. 542.)

In *United States* v. *Jin Fuey Moy*, supra, the words "any person not registered" used in the Harrison Narcotic Act were construed not to mean "any person in the United States" as the context apparently indicated, but to mean "any person" in the class required to be registered by Section 1 of the Act (p. 402).

A statute making it a crime to detain or retard the passage of the mail was construed, notwithstanding the apparently plain words, as inapplicable to the case of an arrest of a carrier of mail for murder (*United States* v. *Kirby*, 7 Wall. 482, 486 [74 U. S.]; see also and cf. *Church of the Holy Trinity* v. *United States*, 143 U. S. 457).

Subdivision (g) of Section 302 of the Act in suit (Revenue Act of 1926) provides for the inclusion in the gross estate of proceeds of life insurance policies:—

> "; * * * to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance taken out by the decedent upon his own life".

Notwithstanding the provisions of the statute which plainly states that if the insurance was taken out by the decedent on his own life all over $40,000 is taxable, the Treasury Department in administering the law construes the statute so as to include the proceeds of life insurance policies payable to designated beneficiaries only "if the decedent possessed at the time of his death any of the legal incidents of ownership". (Reg. 80, Art. 27; see also interpretation by Gen. Counsel Dec. 22, 1934, Commerce Clearing House, F. T. S. for 1935, p. 8046; and compare as a reason, no doubt, for this construction, *Chase National Bank* v. *United States*, 278 U. S. 327.)

We must look to the purpose of the act, taking into consideration the fundamental law governing the scheme of the tax. It was intended to catch within the net of the law all transfers made before death the disposition of which was reserved to the control of the settlor to the time of his death. If, on the other hand, that power or control of the disposition of the property be not in the decedent at the time of his death, it is difficult to see how the transfer could in any substantial or real sense be said to be testamentary in character, or the taxation of such trusts be at all necessary to the full and complete operation of the statute (see and cf. *Nichols* v. *Coolidge*, 274 U. S. 531 and *May* v. *Heiner*, 281 U. S. 238, 243).

The Committee Report itself quoted on page 12 of the petitioner's brief re-affirms this purpose. It is, so far as pertinent hereto: "By this subdivision *if the decedent had the power at the time of his death* to change the enjoyment or property interest * * * such interest is to be included for estate tax purposes in his gross estate" (italics ours). Obviously if he has not the power, or that power be so circumscribed and bridled as to make it in effect a nullity, it cannot within reason be said that the statute was intended by the Congress to have application. The statute was after *pseudo* or *quasi* transfers, not completed acts.

But the Committee Report proceeds further and even indicates what it means by the "power at the time of the death," for it says "Even though the decedent has made the transfer specified in this subdivision, *he has retained substantial control over the disposition of the property* through the power to change the enjoyment thereof * * *" (italics ours). It was the purpose of Congress that before a transfer (which was subject to the gift tax under the 1924 Act) could be included as a part of the decedent's gross estate under Section 302(d), there must be a power in the decedent at the time of his death, and that power must be a "substantial" one, that is, a "substantial control over the disposition of the property".

We think it fairly may be said that it is a far cry to say that the settlor in the case in suit had a power to change the enjoyment of the property or that she retained substantial, if, indeed, any, control over the disposition of it.

The decision of this Court in *Porter* v. *Commissioner*, supra, construing this section, is in exact accord with the purposes as indicated in the Report of the Ways and Means Committee above referred to. In that case there was a power, a substantial control, over the disposition of the property to uses other than those beneficial directly to the grantor, nevertheless, the power was there exercisable at the will of the settlor. On the other hand, if no power exist, or it be not a substantial control, that is, a power exercisable at the will of the settlor, not only, we submit, did the Congress not intend such a transfer to be included as a part of the gross estate of the decedent, but, the language in view of the general law underlying the tax scheme, appropriately should not be so construed.

If the statute may not be given the interpretation which has been attributed to it by all the courts that so far have considered the matter, with the exception of the one case of *Commissioner* v. *Strauss*, 77 F. [2d] 401, then it is clear the statute as applied to the facts in suit is in violation of the due process of law clause of the Fifth Amendment of the Federal Constitution as arbitrary and unreasonable (*Heiner* v. *Donnan*, 285 U. S. 312; *Schlesinger* v. *Wisconsin*, 270 U. S. 230, 240, and cf. *Hoeper* v. *Tax Commission*, 284 U. S. 206).

As the transfer in suit was not made in contemplation of death, and as the settlor had parted with the property before her death, and had no power of revocation, alteration or appointment to new uses, except with the consent of an adverse interest, and had no dominion over, or control of, the disposition of the property in any substantial sense whatever, and as the trust took effect as of the day of its creation, and the rights of the parties at that time became fixed and determined, there was nothing to pass from

her at her death upon which the tax could fasten. So stated the statute is inapplicable and should be so construed. But if construed nevertheless as applying, the statute, we urge, is unconstitutional for the reasons hereinbefore and hereinafter set out.

POINT II.

The statute if construed to apply to the facts in suit is unconstitutional.

The statute imposes an excise upon the transfer of an estate upon the death of the owner (Sec. 301; *May* v. *Heiner*, 281 U. S. 238, 244; *Y. M. C. A.* v. *Davis*, 264 U. S. 47, 50; *Edwards* v. *Slocum*, 264 U. S. 61).

As Mr. Justice Sutherland said in *Heiner* v. *Donnan* (285 U. S. 312) at p. 322:

> "The thing taxed is the transmission of property from the dead to the living. It does not include pure gifts *inter vivos*. The tax rests, in essence, 'upon the principle that death is the generating source from which the particular taxing power takes its being and that it is the power to transmit, or the transmission from the dead to the living, on which such taxes are more immediately rested. * * * It is the power to transmit or the transmission or receipt of property by death which is the subject levied upon by all death duties. *Knowlton* v. *Moore*, 178 U. S. 41, 56, 57.'"

We are here dealing with a death duty, and to justify its imposition there must be a transmission, or the power to transmit or the receipt of property, by virtue of death. Gifts made in contemplation of death are included within the web of the tax scheme "because the transfer is considered to be testamentary in effect" (*Milliken* v. *United States*, 283 U. S. 15, 23), and because the reasons that prompt and motivate such transfers are so assimilated

to death, that in effect it may be said the property passes by virtue of death. But with the exception of such gifts the statute may not bring into the gross estate, within the purview of constitutional limitations, any transfer made *inter vivos* wherein there is nothing of property that passes from the decedent or accrues to the living at or by reason of death.

In estates by the entirety, or joint estates, it has been held (*Tyler* v. *United States*, 281 U. S. 497) that death occasions the shifting of the economic interests and benefits to the survivor, and therefore valuable property rights and assurances pass or accrue by virtue of death. The exercise of powers of appointment by will is the occasion of the transfer of property or the shifting of economic interests at the time of death; transfers, the control of the ultimate disposition of which remain in the power of the settlor until his death, are also appropriately within the power of the Congress, because the death of the decedent terminates the control, ends the possibility of any change by him, and is, in respect of title to the property, the source of valuable assurances passing from the dead to the living (*Porter* v. *Commissioner*, supra, at p. 444).

The Federal estate tax law as a whole comprehends only the passage of property at death or the shifting of economic interests at death or transfers with death as the motivating cause thereof. As Mr. Justice Stone said in *Reinecke* v. *Northern Trust Company*, supra, (at p. 347):

> "In its plan and scope the tax is one imposed on transfers at death or made in contemplation of death and is measured by the value at death of the interest which is transferred. * * * It is not a gift tax, * * *. One may freely give his property to another by absolute gift without subjecting himself or his estate to a tax, but we are asked to say that this statute means that he may not make a gift *inter vivos*, equally absolute and complete, without subjecting it to a tax if the gift takes the form of a life estate in one with remainder over to another at or after the donor's

death. It would require plain and compelling language to justify so incongruous a result and we think it is wanting in the present statute.

It is of significance, although not conclusive, that the only section imposing the tax, § 401, does so on the net estate of decedents, and that the miscellaneous items of property required by § 402 to be brought into the gross estate for the purpose of computing the tax, unless the present remainders be an exception, *are either property transferred in contemplation of death or property passing out of the control, possession or enjoyment of the decedent at his death.*" (Italics ours.)

The transfer by Gertrude Feldman James was not in contemplation of death, concededly. No property passed from her control, possession or enjoyment at her death. She could not appoint to herself nor revoke for her own benefit because there lay athwart any such power the forbidding hand of a substantial beneficial interest in both the income and the principal of the property transferred. She had no more right or power to appoint to other uses than she had to appoint to herself, and no more power or ability to control the disposition of the property than in any other absolute and irrevocable gift *inter vivos*. The obliteration of the life interest in the income that she had is not the occasion of a death duty under the statute in suit (*May* v. *Heiner*, 281 U. S. 238; *Morsman* v. *Burnet*, 283 U. S. 783; *Burnet* v. *Northern Trust Co.*, 283 U. S. 782).

Her act on February 21, 1930, creating the trust and transferring the property, was, so far as her will and power was concerned, final and unalterable. If this be so then there is no more power in the Congress to bring this transfer within the gross estate so as to subject it to tax as a part of the estate of the decedent than there was under the same act the power to bring the gifts of *Donnan*, equally complete and irrevocable, within the gross estate (*Heiner* v. *Donnan*, supra). There is no relation between the estate of Gertrude Feldman James, if any, and this gift which

was completed prior to her death. To impose a tax on this transfer, or upon her estate and include this transfer as a part thereof, when it was not made in contemplation of death, and the transfer was complete long prior to her death, and when she was without any reserved power of control or disposition of the property either beneficial to herself or otherwise, would in effect be to measure the tax upon the estate of this decedent by the value of property belonging to someone else; or to impose a gift tax upon her upon this gift under the guise of a Federal estate tax imposed and operative a long time after the completion of the transfer. This Court has condemned this basis of taxation (see and cf. *Knowlton* v. *Moore*, 178 U. S. 41, 76; *Schlesinger* v. *Wisconsin*, 270 U. S. 230; *Hoeper* v. *Tax Commission*, 284 U. S. 206; *Heiner* v. *Donnan*, 285 U. S. 312; and see also the fundamental doctrine laid down in *Reinecke* v. *Northern Trust Company*, supra).

This is not a gift tax, it is a death tax, and to sustain its application and operation the transfer must be assimilated to death or there must be some property of some sort passing out of the control, possession or enjoyment of the decedent at her death, or because of her death. In fact, a death tax imposed upon anything other than property passing at death or transfers made in contemplation of death as substitutes for testamentary dispositions, is capricious and arbitrary and challenges fair dealing even more so than mere retroactive taxes. (*Heiner* v. *Donnan*, supra, p. 328). As Judge Learned Hand said in *Frew* v. *Bowers* (12 F. [2d] 625, at p. 630):

> "Such a law is far more capricious than merely retroactive taxes. They do indeed impose unexpected burdens, but at least they distribute them in accordance with the taxpayer's wealth. But this section distributes them in accordance with another's wealth; that is a far more grievous injustice."

It is respectfully submitted in view thereof that the trust in suit is not subject to tax under the provisions of Section 302(d), for that section does not mean and was not intended by the use of the words "any person" to comprehend one whose interest was directly adverse to the exercise of any control over the disposition of the property. When one makes a gift outright the transfer becomes complete at that moment. Yet the donee may subsequently agree to return the property upon request of the donor. A person who makes a gift to a donee with the provision that the donor may recall the gift with the consent of the donee, stands in no different position. In both cases the gift is complete and irrevocable so far as the power of the donor to withdraw, or modify, or alter the same is concerned.

Gertrude Feldman James having no property interest to transfer at her death, and having no control over the disposition of the property to other uses and purposes at her death, and the transfer not having been made in contemplation of death, the tax, if imposed upon that transfer, is in violation of the due process of law clause of the Fifth Amendment of the Federal Constitution.

POINT III.

No part of the trust fund is subject to the tax.

Even assuming *Lit* v. *Commissioner* (72 F. [2d] 551, C. C. A. 3), was correctly decided—which is by no means free from doubt—that case is not an authority for the taxation of the trust in suit or any part thereof. This is so because the facts in suit are entirely different. In the *Lit* case the consent necessary to revocation or alteration was in the wife, who had a life estate but no interest in the remainder as such. In the case at bar (1) the husband was made the direct remainderman upon the termination of the trust during his life—whether or not the settlor was alive;

and (2) in the discretion of the trustee the husband might receive the whole of the principal for his education, care, comfort, support or advancement in life (R. 5). In addition to this, the *Lit* case is in conflict with *Reinecke* v. *Northern Trust Co.* and *McCormick* v. *Burnet.*

This same argument, here advanced by the petitioner, under facts not wholly unlike those at bar, was made to the same court that decided the *Lit* case in *Commissioner* v. *Stevens* (decided Sept. 17, 1935, C. C. A. 3, unofficially reported in Commerce Clearing House F. T. S. at p. 10,425), and that court refused to apply the *Lit* decision in a case where the beneficiaries whose consent was necessary to alteration or revocation had an interest in the corpus as well as income, though that interest in part was contingent or potential (see also *Helvering* v. *Helmholz,* 75 F. [2d] 245—No. 14 here).

The argument advanced by the petitioner means no more than that the Commissioner of Internal Revenue thinks this Court should have taxed in *Reinecke* v. *Northern Trust Co.* at least two-fifths of the trust for the wife, and in *McCormick* v. *Burnet* should have taxed at least two-thirds of the value of the property transferred, or that those decisions are to be qualified to that extent. But the basis of those decisions is not the quantum of the adverse interest, but the quality that rendered the settlor helpless to modify or alter.

But significant in the argument presented is the implication, half expressed, that the petitioner feels that the decision of *Reinecke* v. *Northern Trust Company* is controlling in this case—certainly to the extent of the beneficial or adverse interest of the husband. In this we submit the petitioner is right. But that interest in the husband runs to the principal as well as to the income.

This point raised by the petitioner, is, we think, without merit.

Conclusion.

Gertrude Feldman James had no interest in the trust fund that passed from her on her death to the living, nor any actual power over its disposition which terminated at her death, and thus no part of the trust created by her on February 21, 1930, is subject to the Federal estate tax. This being so, we submit the plainly correct decision of the Court below should be affirmed.

Respectfully submitted,

RUSSELL L. BRADFORD,
Attorney for Respondent.

CARL TAYLOR,
GEORGE H. CRAVEN,
MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.